EXECUTIVE SECRETARIAT

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Executive Secretary
1/26/83
Date

3637 (10-81)

OFFICE OF THE SECRETARY OF THE TREASURY
WASHINGTON, D.C. 20220

January 25, 1983

MEMORANDUM FOR THE VICE PRESIDENT
THE SECRETARY OF STATE
THE SECRETARY OF DEFENSE
THE SECRETARY OF AGRICULTURE
THE SECRETARY OF COMMERCE
THE SECRETARY OF THE INTERIOR
THE SECRETARY OF ENERGY
THE DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET
CHAIRMAN, COUNCIL OF ECONOMIC ADVISORS
ASSISTANT TO THE PRESIDENT FOR NATIONAL SECURITY AFFAIRS
ASSISTANT TO THE PRESIDENT FOR POLICY DEVELOPMENT
UNITED STATES TRADE REPRESENTATIVE
✓ DIRECTOR OF CENTRAL INTELLIGENCE

SUBJECT: Senior Interdepartmental Group on International Economic Policy (SIG-IEP)

A meeting of the SIG-IEP is scheduled for Thursday, January 27, at 2:00 p.m., in the Indian Treaty Room (Room 474 Old Executive Office Building).

Agenda items are:

1. Agriculture Issues (butter exports, wheat flour and local-currency butter sales to Egypt and blended credits);
2. Japanese Auto VRA;
3. Alaskan Oil;
4. Economic Summit;
5. Aircraft Sales to Libya; and
6. Coffee Agreement.

Background papers are attached for agenda items 1, 2, and 6. Agenda items 3, 4, and 5 will be subjects of oral reports.

Attendance is limited to principal, plus one.

for Lucille Dickinson
David E. Pickford
Executive Secretary

Attachments

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Status of Flour Sale to Egypt

On January 17, a Memorandum of Understanding was signed in Cairo between USDA's Commodity Credit Corporation and the Egyptian General Authority for Supply Commodities. The understanding commits Egypt to import 1 million tons of U.S. flour commercially over the next 12 to 14 months, in addition to usual imports under PL-480 and either U.S. or foreign donation programs. If they need any larger amount of commercial flour imports than the 1 mmt over the next year, they must come to the U.S. first. In return, CCC has promised to take "necessary measures" to insure that the 1 mmt of U.S. flour is delivered to Egypt at a fixed, flat price of $155 per metric ton, including freight to Egyptian ports. CCC will also provide guarantees for 3-year, commercial-bank credit on the entire 1 mmt.

To bridge the difference between U.S. domestic-market values and the world price level for wheat flour, the CCC will in effect provide an export subsidy to successful bidders for the Egyptian business. The subsidy will take the form of wheat from CCC stocks. CCC will use a competitive bid process to determine which U.S. mills require the least number of bushels of CCC wheat as compensation for their delivery of flour to Egypt at the agreed $155 price. Deliveries are to begin sometime in March.

This new flour trade will largely displace EC flour in the Egyptian market, which alone accounts for about one-third of the world flour trade and over one-half of EC commercial flour exports. Since world flour markets are limited and mostly already supplied by the EC, there will be little if any alternative outlet for the displaced flour. For the U.S., this new trade will add nearly 50 million bushels to total U.S. wheat/wheat flour exports, about roughly 10,000 additional jobs for the economy, and it will mean about $15 million in savings of CCC outlays for storage and interest, should mean roughly $35 million in additional tax revenue resulting from the increased economic activity.

STATUS OF BLENDED CREDIT

On January 11 President Reagan announced a blended credit program of $250 million direct credit and at least $1 billion in CCC export credit guarantees. USDA has received and analyzed many proposals for use of these funds. A set of 14-16 proposals will be presented to the National Advisory Council Staff Committee at a meeting Thursday, January 27 for interagency advice as the first step in implementing the President's announcement. A number of these agreements should be ready to be announced in early February.

Previously an allocation of $100 million direct credit which was blended with at least $400 million in CCC export credit guarantees was authorized.

In summary the first blended credit package was utilized as follows:

Country	GSM-5 Portion Million $	Total Package Million $	Commodities
Morocco	$ 28	$140	Wheat
Egypt	22	110	Wheat, Veg. Oil, Corn
Yugoslavia	12	60	Cotton
Philippines	8	40	Corn, Soybean Meal, Wheat
Pakistan	5	25	Veg. Oil, Soybean Meal
Brazil	12	60	Wheat
Portugal	1	5	Cotton
Yemen	12	60	Wheat, Rice
	$100	$500	

Commodity Designation - Initial Package

Commodity	Metric Tons		Bales
Wheat	2,420,000		
Vegetable Oil	83,000		
Corn	350,000		
Cotton	43,000	or	197,800
Soybean Meal	102,000		
Rice	15,000		
	3,013,000		197,800

In several cases additional straight GSM-102 commercial credit packages were negotiated which would have increased the 4 to 1 ratio. However, countries asked that these be considered separately so that they would not appear to be negotiating packages greater than 4 to 1 when others were obtaining 4 to 1.

STATUS OF EGYPTIAN SALE OF DAIRY PRODUCTS

Last December, FAS received a request from the Egyptian Government to purchase 18,000 metric tons of butteroil, 12,000 metric tons of butter and 12,000 metric tons of cheese from CCC. The dairy products would be made available in Egypt to needy families through private grocers and government food stores at subsidized prices.

Representatives of the Egyptian Embassy have indicated to us that the 30,000 metric tons of butter and butteroil would be additional. The Egyptian Government also requested that CCC accept Egyptian currency as payment for the dairy products. Treasury has agreed to work with us in the use of the currency so that CCC could obtain reimbursement in dollars by other U.S. Government agencies that need Egyptian currency to carry out activities in Egypt.

On January 12, 1982, Acting Secretary Lyng approved our request to negotiate a sale of dairy products to Egypt. While in Egypt last week, Dick Smith and Jim Ross discussed the possibility of a sale of dairy products as follows:

-- FAS offered to sell butter at the middle of the range of $1,625-1,740 MT, butteroil at $2,250-2,400 MT and cheese at $1,400-1,600 MT, all FAS U.S. ports.

-- CCC would accept Egyptian currency payable upon presentation of shipping documents.

-- No restrictions be placed on the use of the currency by the U.S. Government.

-- Delivery within six months after contract signed.

During the meetings, Egyptians made a counteroffer to FAS as follows:

-- Eliminate butteroil.

-- Quantity of butter - 24,000 MT.

-- Price of butter to be $1,500 MT.

-- Quantity of cheese - 12,000 MT.

-- Price of cheese at $1,300 MT.

-- Three years to make payment in Egyptian currency.

-- No interest to apply.

-- Delivery terms F.O.B.

FAS considers the terms of the counteroffer unacceptable and further negotiations necessary. The credit terms would subject the sale to the Cargo Preference Act, the prices offered are somewhat below competitive world prices, and the delivery terms should be F.A.S. rather than F.O.B.

We have sent by air freight samples of butter and processed cheese and these samples are now being cleared through Customs by our Agricultural Counselor. We will air freight a sample of cheddar cheese today, January 25.

JAPANESE AUTOMOBILE EXPORT RESTRAINTS

Issue

The Government of Japan must decide by March 31 whether to extend their current auto export restraints to the United States for the third year. The U.S. auto industry (management and labor) is calling for the extension of the restraint through March 31, 1985 (fourth year), and a rollback in the level of restraint. An options paper is currently being prepared for approval by the TPC/CCCT. Ambassador Brock will raise this issue with the Japanese in detail in early February when he is in Tokyo.

Background

In May 1981, following strong Congressional pressure for a response to an increased Japanese share of U.S. auto market and high unemployment in the domestic industry, the Japanese announced a two year period of automotive export restraints, with a possible third year extension, at 1.68 million autos for the first year of restraint.

We have informed the Japanese that in view of continued low levels of sales (1982 was the worst sales year in 20 years) and high levels of unemployment, (300,000 autoworkers and approximately 600,000 auto parts workers), a third year of restraint, April 1983-March 1984, would be needed. The Japanese are also aware of the 97th Congress' consideration of a domestic content bill which was passed by the House. In addition to the anticipated reintroduction of local content legislation, the United Auto Workers and U.S. auto manufacturing companies have also called for a rollback in the Japanese restraint level in response to unanticipated depressed sales in 1981 and 1982.

Commerce is presently preparing an up-dated analysis of the auto outlook for the U.S. market for the Japanese fiscal year beginning April 1, 1983. This estimate, which should be completed within the next several days, will likely show total auto sales in the United States of just under nine million units (excluding Puerto Rico, but including vans). While an improvement over 1980 and 1981 sales of 8.9 and 8.5 million units, respectively, such an outlook is far below the annual sales of 10 and 11 million units that were achieved from 1976 to 1979.

Currently, in preparation is an options paper which will consider the advantages and disadvantages of various restraint proposals. This paper will be presented next week for TPC/CCCT consideration. Clearly, at least a third year of restraint is necessary for the economic viability of the domestic industry and to head off protectionist legislation.

U.S. Membership in the 1983 International Coffee Agreement

Issue:

Negotiations for a new International Coffee Agreement ended September 24. They resulted in an accord on a new six-year agreement to enter into force October 1, 1983. Should the United States join the new 1983 Agreement?

Advantages:

-- Membership would have important foreign policy benefits: it a) has an important impact on bilateral relations with Brazil, Colombia, Indonesia and the Ivory Coast; all play key regional roles; b) would avoid sharp criticism from developing nations in general; and c) would complement the political benefits of the Caribbean Basin Initiative.

-- The 1983 Agreement is improved along the lines we sought. Continued U.S. membership would encourage evolution in the right direction.

-- U.S. refusal to join would likely doom the Agreement and encourage disgruntled exporters to form a coffee cartel to raise prices. (Such an effort succeeded for a time in 1979-80.)

-- The Agreement might offer benefits in the form of more stable prices and supplies as well as protection against disastrous declines in export earnings.

Disadvantages:

-- The Coffee Agreement requires negotiated government decisions on the source, amount, types, and prices of coffee. Decisions best left to the market.

-- The Agreement's massive market intrusion is at sharp variance with the Administration's free-market philosophy.

-- The Agreement uses export quotas to regulate trade. They are inherently flawed because they provide no, or little, protection against price increases, while providing a cushion against price declines.

-- Country export quotas, in many cases, do not reflect expected export performances. Some countries are unlikely to be able to fill their export quotas, while others could ship more coffee than allowed. Moreover, the quotas permit non-member importing countries (primarily the Soviet Union) to purchase coffee at a discount, since exports to them do not count against quota.

Background:

Based on a TPC mandate the United States entered negotiations for a new Coffee Agreement in January, 1982. The United States sought to make the Agreement more responsive to market signals and to increase consuming country influence in the management of the Agreement's economic provisions. The Agreement relies on annual and quarterly quotas as the mechanisms to regulate the flow of coffee designed to promote price stability. Over the longer term the price range can be adjusted downward or upward as supply and demand trends dictate.

Principal U.S. goals in the negotiation were to 1) improve the annual allocation of export quotas among exporting countries; 2) introduce a system by which export quotas of those coffees in greatest demand could be increased during the year; 3) penalize countries which failed to ship quota amounts; and 4) outlaw collusion among producer countries.

The new Agreement only partially fulfills the U.S. goals, but the Delegation did achieve at least some improvement in those areas we targeted and the new Agreement is better than the expiring one. Importing country influence was enhanced and export allocations among producing countries were improved. However, the United States did not achieve automatic adjustment to market signals -- though the door was left open to changes in that direction -- nor did the United States achieve a meaningful anti-collusion provision. Consequently, export shares -- questionable in any event -- tend to be rigid and access to certain types of coffee may be less than optimal.

The United States was a prime mover behind the first coffee agreement in 1962 as a means of helping Latin America cope with then huge coffee surpluses. From 1972 to September 1980, export quotas were not in effect because of relatively high coffee prices and the inability of consumers and producers to agree on a price range. In the late seventies, certain Latin American coffee producers attempted to raise the price of coffee through purchases and sales in the spot and future markets; that effort collapsed in the face of U.S. opposition and the return of surplus conditions to the market. Quotas were reintroduced in September 1980 and have been in effect since to defend a price range of $1.15 - $1.45 a pound. World coffee prices have largely stayed in the lower part of that range.

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